

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

THE APPLICATION OF JACKSON)
COUNTY RURAL ELECTRIC COOPERATIVE)
CORPORATION OF MCKEE, KENTUCKY,) CASE NO. 8647
FOR AN ORDER AUTHORIZING AN)
INCREASE IN ITS RETAIL RATES,)
APPLICABLE TO ALL CONSUMERS)

O R D E R

On November 15, 1982, Jackson County Rural Electric Cooperative Corporation ("Jackson County") filed an application with this Commission requesting to increase its annual revenue by \$1,355,900, or 6.69 percent. Jackson County stated that the proposed rate adjustment was required due to increased operating expenses, higher interest rates, and declining growth in sales, all of which have contributed to reduced margins.

On November 22, 1982, the Consumer Protection Division in the office of the Attorney General moved to intervene in this proceeding pursuant to KRS 367.150(8), which motion was granted. No other parties appeared to formally intervene herein. The Commission scheduled a public hearing on the matter and directed Jackson County to give notice to its consumers of the proposed rates and the hearing scheduled for March 15, 1983.

This Order addresses the Commission's findings and determinations on issues presented and disclosed in the hearing and investigation of Jackson County's revenue requirements and

rate design. Jackson County has been granted the full increase requested of \$1,355,900.

COMMENTARY

Jackson County is a consumer-owned rural electric cooperative engaged in the distribution and sale of electric energy to approximately 30,250 member-consumers in the southeastern Kentucky counties of Breathitt, Clay, Estill, Garrard, Jackson, Laurel, Lee, Leslie, Lincoln, Madison, Powell, Pulaski, Rockcastle, and Wolfe. Jackson County purchases all of its electric energy from East Kentucky Power Cooperative, Inc. ("East Kentucky").

TEST PERIOD

Jackson County proposed and the Commission has accepted the 12-month period ending June 30, 1982, as the test period for determining the reasonableness of the proposed rates. In utilizing the historic test period, the Commission has given full consideration to appropriate known and measurable changes.

VALUATION

Net Investment

Jackson County proposed a net investment rate base of \$27,298,898. The Commission concurs with this determination with the following exceptions:

Jackson County proposed several adjustments to plant in service and construction work in progress ("CWIP") to reflect changes occurring after the test year. These included transfers from CWIP to plant in service in the amount of \$190,691 and adjustments to increase CWIP by \$38,287 to include the effects of

the portion of pro forma expense adjustments charged to construction.

The Commission's objective in establishing the year-end rate base is to determine the value of Jackson County's plant devoted to public use at the end of the test year. Jackson County did not propose to adjust operating revenues and expenses associated with the additions of new facilities. Therefore, in accordance with past practice, the Commission will not allow the post test period adjustments to plant in service and CWIP.

The Commission has adjusted the accumulated provision for depreciation to reflect the pro forma adjustment to depreciation expense found reasonable herein. Also, the provision for working capital has been adjusted to reflect the pro forma adjustments to operation and maintenance expenses allowed herein for rate-making purposes.

Based on the Commission's adjustments, Jackson County's net investment rate base found reasonable for rate-making purposes is as follows:

Utility Plant in Service	\$33,946,032
Construction Work in Progress	<u>209,460</u>
Total Utility Plant	\$34,155,492
Add:	
Materials and Supplies	\$ 453,635
Prepayments	138,860
Working Capital	<u>348,401</u>
Subtotal	\$ 940,896
Deduct:	
Depreciation Reserve	\$ 8,238,494
Customer Advances for Construction	<u>413,017</u>
Subtotal	\$ 8,651,511
Net Investment	<u>\$26,444,877</u>

Capital Structure

The Commission finds from the evidence of record that Jackson County's capital structure was \$30,281,697 and consisted of \$8,695,650 in equity and \$21,586,047 in long-term debt. In this determination of the capital structure, the Commission has excluded accumulated generation and transmission capital credits in the amount of \$978,834.

REVENUES AND EXPENSES

Jackson County proposed several adjustments to revenues and expenses to reflect more current and anticipated operating conditions. The Commission finds the proposed adjustments are generally proper and acceptable for rate-making purposes with the following modifications:

Revenue Normalization

Jackson County proposed an adjustment of \$1,465,805 to normalize its test year revenue from sales to reflect a full year's sales at the rates in effect at the time the application was filed. Since the filing of the application, Jackson County has incurred an increase in its wholesale power costs from East Kentucky, approved by the Commission in Case No. 8648, Adjustment of Rates for Wholesale Electric Power to Member Cooperatives of East Kentucky Power. In order for Jackson County to recover this additional cost, the Commission approved a rate increase, effective April 1, 1983, in flow-through Case No. 8662. To reflect that increase in this case, the Commission has made a

further adjustment to increase operating revenue by \$1,885,614, resulting in a total adjustment of \$3,351,419.

Purchased Power Adjustment

Jackson County proposed an adjustment of \$1,466,648 to normalize its purchased power cost for the test year based on the wholesale power rate in effect at the time the application was filed. To reflect the increase in Jackson County's power cost from East Kentucky's wholesale rate increase in Case No. 8648 the Commission has further increased the proposed adjustment by \$1,885,239 resulting in a total adjustment of \$3,351,887.

Fuel Clause

The Commission adjusted Jackson County's base rates in Case No. 8606, Examination of the Fuel Adjustment Clause of Jackson County Rural Electric Cooperative Corporation, to roll in the fuel cost of its wholesale power supplier. Jackson County's fuel adjustment clause contains a provision which allows total recovery or refund of fuel adjustment charges or credits. Therefore, the Commission has decreased revenue by \$460,946 and decreased purchased power expense by \$483,636 to exclude the fuel revenue and cost actually incurred during the test year in the determination of revenue requirements.

Customer Records and Collection Expense

During the test year Jackson County's recorded expense for Account 903, Customer Records and Collection Expense, was \$367,838. In response to an information request Jackson County indicated that amounts totalling \$12,712 for computer charges and payments to a collection agency which were charged to expense

during the test period were actually applicable to prior reporting periods. Therefore, the Commission has made an adjustment to reduce operating expenses by \$12,712 to eliminate these items for rate-making purposes.

Administrative and General Salaries

Jackson County's administrative and general salaries for the test year totalled \$199,092. In response to an information request Jackson County indicated that \$2,512 was improperly recorded as expense that should have been included in other deferred charges. The Commission has, accordingly, made an adjustment of \$2,512 to reduce operating expenses and eliminate this item for rate-making purposes.

Depreciation Expense

Jackson County proposed an adjustment of \$47,407 to increase depreciation expense based on the year-end level of plant in service plus the transfer of \$190,691 from CWIP to plant in service discussed in the section on net investment. As discussed previously, the Commission has not accepted the transfer from CWIP to plant in service. Therefore, the proposed adjustment to depreciation expense has been reduced by \$5,630 to \$41,777 to reflect the annual expense for the year-end level of plant in service.

Public Service Commission Assessment

During the test year Jackson County incurred \$13,733 in expense for the regulatory assessment to fund the work of this Commission. Based on the 1982 assessment of \$19,612, Jackson

County proposed an adjustment of \$5,879 to reflect the increased expense.

The Commission will not accept the proposed adjustment due to changes in calculating the assessment for rural electric cooperatives enacted by the 1982 Kentucky General Assembly. These changes will reduce the revenue base on which the assessment is calculated by one-half of purchased power expense. While that calculation is easily made, there is no way of determining the future assessment rate or the amount of the future assessment. Therefore, the Commission will not accept an adjustment to the regulatory assessment expense, but will allow the actual test year expense for rate-making purposes.

Legal Expenses

During the test year Jackson County incurred \$7,500 in expense for legal fees as the result of a personal injury lawsuit filed against it. The Commission is of the opinion that personal injury claims such as the one brought against Jackson County during the test year are infrequent, non-recurring events and that the related expenses are non-recurring and extraordinary. Therefore, the Commission has made an adjustment to reduce Jackson County's operating expenses by \$7,500 for rate-making purposes.

Directors' Expenses

The directors of Jackson County are provided compensation for actual expenses incurred while in attendance at industry association meetings. In addition, Jackson County provides a meeting fee of \$150 for directors attending meetings of industry associations on whose boards they serve. Jackson County also

provides a \$75 meeting fee for attendance at other association meetings. The Commission is of the opinion that the directors should be reimbursed only for the necessary and reasonable costs incurred and that the fees for attending industry association meetings are excessive and unreasonable. Therefore, the Commission has reduced directors' expenses by \$3,375 to exclude the amount of these fees paid during the test year.

Interest Expense on Long-Term Debt

Jackson County proposed an adjustment of \$178,313 to increase its long-term interest expense to reflect the year-end levels of long-term debt and the advance of an additional \$721,000 scheduled to occur in August 1982. Based on the additional advances and retirements of debt that have occurred through January 1983, the Commission has made an adjustment of \$234,152 to the test year expense to reflect the increased interest expense.

Interest Income

During the test year Jackson County had interest earnings on its investments of \$214,439. \$150,029 of this amount was earned on commercial paper issued by the National Rural Utilities Cooperative Finance Corporation ("CFC"). Jackson County proposed an adjustment of \$59,952 to reduce interest income based on the recent decline in interest rates for commercial paper. The Commission is of the opinion that such an adjustment can not be properly made based on changes in interest rates while ignoring the amounts and length of time of the investment. This opinion is supported by Jackson County's experience since the end of the test year. During a period of declining interest rates, Jackson

County's interest income for the 12 months ended January 31, 1983, was \$219,560, which is slightly greater than the test year interest income.

The Commission is of the opinion that the proposed adjustment does not adequately consider the various factors that affect the amount of interest income. Therefore, the proposed adjustment has been rejected and the actual test year interest income included in the determination of revenue requirements.

The effect of the accepted pro forma adjustments on net income is as follows:

	<u>Actual Test Period</u>	<u>Pro forma Adjustments</u>	<u>Adjusted Test Period</u>
Operating Revenues	\$19,487,468	\$2,898,417	\$22,385,885
Operating Expenses	18,089,000	3,045,900	21,134,900
Operating Income	<u>\$ 1,398,468</u>	<u>\$ (147,483)</u>	<u>\$ 1,250,985</u>
Interest on Long-term Debt	1,047,423	234,152	1,281,575
Other Income and (Deductions)-Net	<u>337,269</u>	<u>(132,219)</u>	<u>205,050</u>
Net Income	<u>\$ 688,314</u>	<u>\$ (513,854)</u>	<u>\$ 174,460</u>

REVENUE REQUIREMENTS

The actual rate of return of Jackson County's net investment rate base established herein for rate-making purposes was 5.29 percent. After taking into consideration the accepted pro forma adjustments, Jackson County would realize a rate of return of 4.73 percent. The Commission is of the opinion that the adjusted rate of return is inadequate and a more reasonable rate of return would be 9.86 percent. In order to achieve this rate of return Jackson County should be allowed to increase its

annual revenue by approximately \$1,355,900 which would produce a Times Interest Earned Ratio of 2.19. This additional revenue will provide net income of \$1,530,360 which should be sufficient to meet the requirements in Jackson County's mortgages securing its long-term debt.

REVENUE ALLOCATION AND RATE DESIGN

Jackson County did not propose any changes to its current rate schedule or to its tariff regulations. Jackson County used the percentile method to allocate the revenue and to increase the rate steps. The Commission is of the opinion that in this case the percentile method is most appropriate for the ratepayers of Jackson County. Additionally the Commission has adjusted Jackson County's normalized revenue to include the rates approved in Case No. 8662.

OTHER ISSUES

Utility Management

Jackson County is among the largest of the electric distribution cooperatives regulated by this Commission and, as such, benefits from certain economies of scale. As a result, Jackson County's cost per consumer is the lowest of all Kentucky cooperatives.¹ The Commission is encouraged by Jackson County's favorable results; however, based on recent cost increases, the Commission questions the extent to which Jackson County's efforts to control costs have influenced these results.

¹ Direct testimony of Lee Roy Cole, page 11 of 13.

During the test year Jackson County's variable operating expenses, exclusive of purchased power, totalled \$2,679,071.² This represents an increase of 38.5 percent over the level of expense, \$1,933,704, incurred 2-1/2 years earlier in 1979. Although it is aware of increases in the cost of labor and insurance, increases over which Jackson County does not have complete control, the Commission looks with concern at the cost increases Jackson County has incurred in recent years. With recent declines in the rate of inflation, the Commission is hopeful that Jackson County can effect some moderation of these cost increases.

Directors' Fees

The nine members of Jackson County's board of directors each receive \$150 as compensation for attendance at each monthly meeting of the board. This fee, which was \$80 as recently as 1980, has nearly doubled over the past 3 years. Mr. Lee Roy Cole, Jackson County's President and General Manager, indicated that these fees were above average for distribution cooperatives within Kentucky. Mr. Cole further stated that the directors themselves set the fees without any input from other sources.

The Commission finds it surprising that the directors of Jackson County would increase their fees by this amount at a time when Jackson County is attempting to control costs and operate more efficiently. The Commission is hopeful that these

² Ibid., page 4.

fees have reached a level at which they will stabilize, rather than continue to escalate as they have in recent years. Whether they stabilize will be a reflection of the board's concerns toward controlling costs.

SUMMARY

The Commission, having considered the evidence of record and being advised, is of the opinion and finds that:

1. The rates in Appendix A are the fair, just and reasonable rates for Jackson County and will produce gross annual revenue sufficient to pay its operating expenses, service its debt and provide a reasonable surplus for equity growth.

IT IS THEREFORE ORDERED that the rates in Appendix A be and they hereby are approved for service rendered by Jackson County on and after the date of this Order.

IT IS FURTHER ORDERED that within 30 days from the date of this Order Jackson County shall file with the Commission its revised tariff sheets setting out the rates approved herein.

Done at Frankfort, Kentucky, this 3rd day of May, 1983.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:

Secretary

APPENDIX

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE
COMMISSION IN CASE NO. 8647 DATED May 3, 1983.

The following rates and charges are prescribed for the customers in the area served by Jackson County Rural Electric Cooperative Corporation. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under authority of this Commission prior to the effective date of this Order.

SCHEDULE 10

RESIDENTIAL, FARM AND NON-FARM SERVICE*

Rate

Customer Charge Per Month - Includes No KWH Usage	\$4.85
First 650 KWH Per Month	.06512
All Over 650 KWH Per Month	.05573

SCHEDULE 20

COMMERCIAL, SMALL POWER, AND THREE-PHASE FARM SERVICE*

Rate

Customer Charge Per Month - Includes No KWH Usage	\$5.35
First 1,000 KWH Per Month	.06699
Next 1,000 KWH Per Month	.06538
All Over 2,000 KWH Per Month	.06252

SCHEDULE 30

LARGE POWER SERVICE LESS THAN 50 KW*

Rate

Customer Charge Per Month - Includes No KWH Usage	\$6.40
Demand Charge Per KW of Demand	4.87
<u>Energy Charge Per KWH</u>	
First 1,000 KWH Per Month	.05909
All Over 1,000 KWH Per Month	.05587

Minimum Monthly Charge

The minimum monthly charge shall be the minimum monthly charge specified in the contract, or the minimum monthly charge, or \$1.20 per KVA of installed transformer capacity, or \$37.00, whichever amount shall be the greatest.

SCHEDULE 33 WATER PUMPING SERVICE*

Rate

Customer Charge Per Month - Includes No KWH Usage	\$10.70
First 10,000 KWH Per Month	.05882
Next 40,000 KWH Per Month	.05638
All Over 50,000 KWH Per Month	.05264

Minimum Monthly Charge

The minimum monthly charge shall be the minimum monthly charge specified in the contract, or the minimum monthly charge, or \$1.20 per KVA of installed transformer capacity, or \$37.00, whichever amount shall be the greatest.

SCHEDULE 40 LARGE POWER MORE THAN 50 KW BUT LESS THAN 275 KW*

RATE

Customer Charge Per Month - Includes No KWH Usage	\$16.20
Demand Charge Per KW of Demand	4.87

Energy Charge

First 10,000 KWH Per Month	.05239
Next 40,000 KWH Per Month	.05098
All Over 50,000 KWH Per Month	.04897

Minimum Monthly Charge

The minimum monthly charge shall be the minimum monthly charge specified in the contract, or the minimum monthly charge, or \$1.20 per KVA of installed transformer capacity, or \$37.00, whichever amount shall be the greatest.

SCHEDULE 43 LARGE POWER RATE - OVER 275 KW*

Rate

Customer Charge Per Month - Includes No KWH Usage	\$32.00
Demand Charge Per KW of Demand	4.87

Energy Charge

First	150,000 KWH Per Month	.04797
All Over	150,000 KWH Per Month	.04625

Minimum Monthly Charge

The minimum monthly charge shall be the minimum monthly charge specified in the contract, or the minimum monthly charge, or \$1.20 per KVA of installed transformer capacity, or \$37.00, whichever amount shall be the greatest.

SCHEDULE 50 AND 60
SCHOOLS, CHURCHES AND COMMUNITY HALLS*

Rate

Customer Charge Per Month - Includes No KWH Usage	\$5.35
First 800 KWH Per Month	.05887
All Over 800 KWH per Month	.05631

SCHEDULE SL
OUTDOOR LIGHTING SERVICE - SECURITY LIGHTS*

Rate Per Light Per Month

Mercury Vapor Lamp	175 Watt	90 KWH	\$5.65
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SCHEDULE 52
ALL ELECTRIC SCHOOLS

Rate

Customer Charge Per Month - Includes No KWH Usage	\$10.70
All KWH	.05480

Minimum Charge

The minimum annual charge will be not less than \$14.40 per KVA or required transformer capacity as determined by the Cooperative.

*Fuel Clause Adjustment

All rates are applicable to the Fuel Adjustment Clause and may be increased or decreased by an amount per KWH equal to the fuel adjustment amount per KWH as billed by the Wholesale Power Supplier plus an allowance for line losses. The allowance for line losses will not exceed 10% and is based on a twelve-month moving average of such losses. This Fuel Clause is subject to all other applicable provisions as set out in 807 KAR 5:056.